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SIPDIS

TREASURY FOR FTAT, OCC/SIEGEL, AND OASIA/ICB/ATUKORALA
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E.O. 12958: N/A

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SUBJECT: Austrian Government Bank Rescue - Update

REF: (A) VIENNA 1665; (B) VIENNA 1619 and previous

¶1. SUMMARY: As expected, more large Austrian banks (Raiffeisen Zentralbank, Volksbank, and Hypo Alpe Adria) have applied for GoA equity injections; no insurer has showed interest so far. Volksbanken AG, after its Kommunalkredit flop and other write-offs, will likely show a loss for 2008. Hypo Alpe Adria bank (HAA) has a low equity ratio and problems stemming from troubled majority shareholder Bayerische Landesbank. The Austrian Financial Market Authority (FMA) is endorsing GoA equity injections and monitoring whether foreign owners plan to withdraw capital from Austrian banks. Credit is still scarce, even with GoA-guaranteed interbank lending auctions underway (an EUR 85 billion program). The GOA's EUR 15 billion equity injection program has not yet received EU Commission approval and has not paid out a single Euro. Banks complain that regulators are trying tack on conditions to equity contracts and have not defined the role of FIMBAG (which will administer GoA funds).
END SUMMARY.

More Banks Resort to State Capital

¶2. After Erste Bank's request for state equity (reftels), on November 25 Raiffeisen Zentralbank (RZB) decided to raise about EUR 2 billion in fresh equity in form of participation shares. Existing shareholders will raise EUR 700 million, with RZB requesting GoA capital for the rest.

¶3. Volksbanken is negotiating with the GoA for participation capital of about EUR 1 billion to bring its Tier 1 capital ratio up to 9%. Volksbanken will try to secure the entire amount from the GoA: no equity increase by existing shareholders is planned, rather current shareholders would at a later date buy the GoA's stake in the form of common shares. Volksbanken faces a difficult period and will likely show a net loss for 2008 due to its Kommunalkredit debacle (prompting write-offs of almost EUR 400 million) and losses of at least EUR 300 million from business with Lehman Brothers, Iceland, and structured products.

¶4. Another problem bank is Hypo Alpe Adria (HAA -- Austria's sixth largest bank) which has made headlines repeatedly in recent years due to scandals and high-risk ventures. Since mid-2007, HAA's majority shareholder (at least 57.5%) is now troubled Bayerische Landesbank. Other shareholders include the Carinthia provincial government (16%), Grazer Wechselseitige insurance (26.5%). With its Tier 1 capital ratio reportedly only 5.6%, HAA needs EUR 2

billion of which EUR 1.3 billion would come from the GoA and EUR 700 million from current owners. The Bavarian state government's rescue package for Bayerische Landesbank reportedly includes fresh equity for HAA (its largest foreign subsidiary), but since one of the Bavarian government's conditions is a massive cut-back of Bayerische Landsbank's international business, rumors are that it may try to sell HAA.

15. So far, no insurance company has shown interest in GoA money. Speaking for one of Austria's three largest insurers, Uniqa CEO Konstantin Klien recently remarked that 8% is too high a price.

16. Austrian Financial Market Authority (FMA) co-CEO Helmut Ettl has suggested that most or all large Austrian banks could tap the GoA EUR 15 billion pot -- since the market is demanding higher capital ratios -- but opposes expanding GoA protection to related industries such as funds. The FMA does not see signs that foreign owners want to withdraw capital from Austrian banks, but is monitoring the situation. NOTE: Ettl's remark primarily concerns BAWAG (100% owned by U.S. fund Cerberus Capital Management) and Bank Austria (97% owned by the Italian UniCredit group), and Hypo Alpe Adria cited above. END NOTE.

Show Us the Money

17. Even though auctions have started under the EUR 85

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billion guarantee of interbank lending, entrepreneurs say loans are unavailable or very difficult to get. Austrian National Bank Governor Ewald Nowotny has also said that credit availability remains a pressing problem.

18. The GoA's EUR 15 billion equity injection program has not paid out a single Euro, even though the GoA decided on it six weeks ago and Parliament approved it October 21. The GoA is still waiting for EU Commission approval after a reported communication breakdown between Brussels and the Austrian Ministry of Finance (MoF) and the Commission's reported questioning of the fixed annual interest of 8% as too low. RZB CEO Walter Rothenteiner, chairman of Federal Economic Chamber's Banking and Insurance Division, complained publicly that if the package "does not kick in soon, the whole thing was not really helpful."

COMMENT-----

19. Frictions over GoA capital participation extend beyond the marked delays. Bank interlocutors say regulators are trying to attach more and more conditions into equity participation contracts. Unclear is the role of the new FIMBAG, created to administer GoA funds (ref A). FIMBAG co-head Hannes Androsch, a respected Social Democratic industrialist, has signaled that FIMBAG will take an activist role -- something banks will probably resist. With Austrian bank holdings in southeastern/eastern Europe (about \$290 billion) now weakening, now is not the time for an ideological battle over state interference, especially if it keeps the GoA from delivering on its existing promise to shore up bank capital. END COMMENT.

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